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Cases, Regulations and Statutes

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FOOTNOTES

1 I.R.C. § 2503. See generally 6 Harl, *Agricultural Law* § 46.04[1] (1993); Harl, *Agricultural Law Manual* § 6.01 (1993).
2 Treas. Reg. §§ 25.6019-1, 25.6075-1.
3 I.R.C. § 2503(b).
4 *Id*.
5 See n. 2 *supra*.
6 See I.R.C. §§ 2503, 2505.
7 Rev. Rul. 71-443, 1971-2 C.B. 337. See Ltr. Rul. 7935115, May 31, 1979 (transfer of corporate stock to issuing corporation); Ltr. Rul. 8422015, Feb. 15, 1984 (same).
8 See Stark v. U.S., 345 F. Supp. 1263 (W.D. Mo. 1972), *aff'd*, 477 F.2d 131 (8th Cir. 1973).
9 Wooley v. U.S., 90-1 U.S.T.C. ¶ 60,013 (S.D. Ind. 1990).
10 McClure v. U.S., 79-2 U.S.T.C. ¶ 13,319 (Ct. Cl. 1979).
11 Maryland Nat'l Bank v. U.S., 609 F.2d 1078 (4th Cir. 1979).
12 McManus v. Comm'r, T.C. Memo. 1980-296, *aff'd*, 82-1 U.S.T.C. ¶ 13,456 (6th Cir. 1982).
13 See Rev. Rul. 75-415, 1975-2 C.B. 374.
14 Crummey v. Comm'r, 397 F.2d 82 (9th Cir. 1968).
15 *Id*.
16 Ltr. Rul. 8006048, Nov. 16, 1979.
17 Ltr. Rul. 8022048, March 4, 1980 (trust contribution two days before the end of calendar year; annual exclusion allowed because donor was natural guardian of minor and local law permitted natural guardians to exercise withdrawal rights); Ltr. Rul. 8308033, Nov. 23, 1982 (each beneficiary had unrestricted right for 30 days to withdraw; annual exclusion available if notice given and no impediment to appointment of guardian under local law). See Rev. Rul. 73-405, 1973-2 C.B. 321 (gift tax annual exclusion allowed even though no fiduciary appointed; no impediment in trust or local law to appointment).
18 Est. of Cristofani v. Comm'r, 97 T.C. 74 (1991), *acq. in result only*, 1992-1 C.B. 1 (right to withdraw limited to 15 days after property contributed to trusts). See AOD 1992-09 (IRS will deny exclusions for powers held by individuals who either have no property interests in trusts except for *Crummey* powers or hold only contingent remainder interests). Compare Ltr. Rul. 9141008, June 24, 1991 (annual exclusion not allowed for grandchildren as remote contingent beneficiaries with limited demand rights).
19 Naumoff v. Comm'r, T.C. Memo. 1983-435; Ltr. Rul. 8485004, June 27, 1984 (same). See also Ltr. Rul. 8433024, May 10, 1984 (present interest in trust transferred where beneficiary had power to demand interest and contributions to trust from past year on annual basis).
20 Est. of Kolker v. Comm'r, 80 T.C. 1082 (1983) (each beneficiary living on donor's birthday to receive distribution from trust).
21 Karpf v. Karpf, 240 Neb. 302, 481 N.W.2d 891 (1992) (no damages, however).
22 See Ross v. Comm'r, 652 F.2d 1365 (9th Cir. 1981) (provision that interest passed to "heirs at law" rather than to donee's estate made annual exclusion unavailable).
23 Treas. Reg. § 25.2503-4(b)(1). See Illinois Nat'l Bank of Springfield v. U.S., 91-1 U.S.T.C. ¶ 60,063 (C.D. Ill. 1991) (substantial restriction existed because trust limited use of funds to education and disability; annual exclusion not allowed).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL

ADMINISTRATIVE EXPENSES. A creditor who had sold cattle feed to the debtor during the bankruptcy case, sought payment as an administrative expense under Section 506(c) for the feed from the proceeds of the sale of the cattle. A creditor with a security interest in the cattle objected, arguing that only a trustee had the authority to seek administrative expense status for expenses used to preserve collateral. The court held that creditors also have standing to seek administrative expense status for property used to preserve collateral. However, the court also held that because the creditor had not filed an adversary proceeding under Bankr. Rule 7001 and no evidence had been presented as to whether the feed was a reasonable and necessary expense which benefitted the secured creditor, the proceeds would be paid to the trustee pending the filing of an adversary proceeding. ***In re* Blaisure, 150 B.R. 343 (Bankr. M.D. Pa. 1992)**.

AVOIDABLE TRANSFERS. In December 1988, the debtor executed an agreement to purchase a one-half interest in a horse owned by a creditor. The purchase agreement granted the seller a security interest in the debtor's interest in the horse to secure the purchase price which was to be paid over six years. The financing statement was not filed until May 1991, less than 90 days before the debtor filed for bankruptcy. The court held that the perfection of the security interest was an avoidable transfer. ***In re* Calumet Farm, Inc., 150 B.R. 403 (Bankr. E.D. Ky. 1992)**.

DISCHARGE-*ALM* § 13.06.* The creditor sold produce to a corporation in which the debtor was the president, principal shareholder and bookkeeper. The creditor filed a notice of the claim with the USDA to preserve its rights in the PACA trust and obtained a default judgment against the corporation. The creditor sought to have the claim declared nondischargeable for defalcation while acting in a fiduciary duty. The court held that the debtor was a fiduciary as to the PACA trust as a responsible person in the corporation and the failure to preserve the trust for creditors was defalcation making the debt nondischargeable. ***In re* Harper, 150 B.R. 416 (Bankr. E.D. Tenn. 1993)**.

EXEMPTIONS-*ALM* § 13.03[4].

AVOIDABLE LIENS. The debtor claimed a homestead exemption and sought to avoid judicial liens against the homestead as impairing the exemption. The Ohio exemption provided an exemption for a homestead only upon a judicial sale of the homestead. The debtor argued that *Owen v. Owen, 111 S.Ct. 1833 (1991)* required that the judicial liens be avoided. The court held that *Owen* did not apply because the debtor had no exemption right until a judicial sale occurred, whereas in *Owen*, the debtor had a right to the exemption as of the bankruptcy filing but the state exemption law attempted to remove the exemption as to judicial liens. ***In re* Braverman, 150 B.R. 681 (Bankr. S.D. Ohio 1993)**.

CONVERSION. Within one month prior to filing for bankruptcy, the debtors sold several non-exempt, non-attached properties and purchased exempt property. A creditor had just obtained a judgment against the debtors but was unable to attach any of the property before the bankruptcy case was filed. The court held that under these circumstances, the transfer of non-exempt assets into exempt assets was fraudulent and denied the exemption as to the converted property. ***In re* Scwarb, 150 B.R. 470 (Bankr. M.D. Fla. 1992)**.

HOMESTEAD. Prior to filing for bankruptcy, the debtor had filed for divorce. The marital property included a residence to which only the debtor's spouse had title. The debtor and spouse both filed for bankruptcy and the cases were jointly administered but not consolidated. After the case was filed, the divorce was granted and the debtor received a one-half interest in the residence. The debtor claimed a homestead exemption in this portion of the residence. The court held that the debtor interest in the residence was only as an unsecured creditor and that the debtor's exemption was limited to the amount recoverable from the spouse's bankruptcy estate. ***In re* McCulley, 150 B.R. 358 (Bankr. M.D. 1993)**.

HOUSEHOLD GOODS. The debtor filed a list of 1,553 items of property as exempt under La. Rev. Stat. § 13:3881. The court held that the exemptions would not be allowed because the list was filed in bad faith since most of the items were not entitled to an exemption, but the court allowed the debtor to amend the schedule, with the warning that failure to remove items not reasonably entitled to an exemption could result in denial of all claimed exemptions. **Ward v. Turner, 150 B.R. 378 (E.D. La. 1993)**.

OBJECTIONS. The debtor claimed an exemption for pension and profit sharing plans and an interest in an IRA. No creditor filed a timely objection to the exemptions but one creditor filed a late objection to the exemption of the plans and IRA. The court held that under *Taylor v. Freeland & Kronz, 112 S.Ct. 1644 (1992)*, the failure to timely object to a claimed exemption was an absolute bar to consideration of the merit of the exemption. ***In re* Kazi, 985 F.2d 318 (7th Cir. 1993), *aff'g unrep. D. Ct. dec. aff'g*, 125 B.R. 981 (Bankr. S.D. Ill. 1991)**.

SALE OF ESTATE PROPERTY. The debtor owned a one-half interest in a stallion and sought court permission to sell the horse free of the other co-owners' interests with the owners receiving their share of the proceeds. The other owners objected, arguing that the sale of the horse would decrease the value of their interests. The court held that the sale could be allowed if (1) the partition of the property "in kind" was not feasible and (2) the benefit to the estate was greater than the detriment to the other owners. The court calculated the benefit/detriment as follows: (1) the debtor's benefit equalled the proposed sale price of the entire interest in the horse less the estimated price of selling only the one-half interest in the horse; the other owners' detriment equalled their loss of income from the sale of their interests less their after tax share of the proceeds of the sale of the entire interest in the horse. The court established a minimum price for the horse which produced 10 cents more benefit to the debtor than detriment to the other owners and held that under Section 363(h) that was enough to authorize the sale at that minimum price or higher. ***In re* Calumet Farm, Inc., 150 B.R. 664 (Bankr. E.D. Ky. 1992)**.

CHAPTER 12

TRUSTEE FEES-*ALM* § 13.03[8]. The debtors' Chapter 12 plan provided for payment of the trustee's fees except where direct payments to creditors were made. The plan also provided that the debtor would make all disbursements under the plan except for payments required to be made by the trustee. The trustee argued that the trustee fee was required to be paid on all payments under the plan on impaired claims, even those directly paid by the debtors. The debtors argued that the plan allowed direct payment of impaired claims; therefore, no fee was due for these direct payments. The court held that under Section 586, payments on impaired claims are made under the plan and require payment of the trustee's fee. ***In re* Wagner, 150 B.R. 753 (Bankr. D. N.D. 1993)**.

During the administration of the debtor's Chapter 12 plan, the Attorney General set the trustee's fee at 11.111111 percent of all plan payments. The rate was based on the interpretation of 28 U.S.C. § 586(e)(1) to include payment of the trustee's fees as a plan payment also subject to the trustee fee. Thus, the maximum rate of 10 percent was charged against the debtor's payments of the trustee's fees. The court held that the 11.111111 percent rate exceeded the statutory maximum of 10 percent and ordered return of fees assessed in excess of 10 percent. ***In re* BDT Farms, Inc., 150 B.R. 795 (Bankr. W.D. Okl. 1993)**.

FEDERAL TAXATION

AUTOMATIC STAY. The debtor incurred post-petition federal tax liability and the IRS levied against the debtor's post-confirmation wages in excess of the wages committed to the funding of the Chapter 13 plan. The debtor sought sanctions against the IRS for violation of the automatic stay. The court held that because all estate property vested in the debtor upon confirmation, the levy did not violate the automatic stay because the wages levied against were not committed to payment for the Chapter 13 plan. ***In re* Markowicz, 150 B.R. 461 (Bankr. D. Nev. 1993)**.

AVOIDABLE LIENS. The IRS filed a claim based upon an unsecured tax lien and the Chapter 11 debtor sought to avoid the unsecured tax lien under Section 506. The bankruptcy court had ruled that the tax lien was avoidable because *Dewsnup v. Timm, 112 S.Ct. 773 (1992)* was applicable only in Chapter 7 cases. The appellate court reversed, holding that Dewsnup applied to all bankruptcy cases and prohibited the avoidance of allowed unsecured claims. ***In re* Blue Pacific Car Wash, Inc., 150 B.R. 434 (W.D. Wis. 1992)**.

AVOIDABLE TRANSFERS. Just prior to the debtor's filing for bankruptcy, the IRS filed tax liens against the debtor and levied against the debtor's interest in two IRA's. The money in one account was paid before the filing but the money in the other account had not been paid. The debtor sought avoidance of the first as a preferential transfer and avoidance of the second lien as impairing an exemption.

The court held that the action against the first levy was barred by government immunity because the debtor sought a return of money, but the action against the second levy was not barred because no money had yet been paid. The court also held that the second lien was not avoidable because the lien would survive discharge of the underlying taxes and could be enforced against exempt property after the case was closed. ***In re* Quillard, 150 B.R. 291 (Bankr. D. R.I. 1993)**.

PASSIVE ACTIVITY LOSSES-*ALM* § 13.03[7]. The court ruled that a debtor's prepetition passive activity losses do not pass to the bankruptcy estate but remain with the debtor. ***In re* Antonelli, 150 B.R. 364 (Bankr. D. Md. 1992)**. Note: the IRS has now issued proposed regulations which include passive activity losses in the list of tax items which pass to the bankruptcy estate in Chapters 7 and 11 (see Vol. 3, *Agric. L. Dig.*, p. 191).

REFUND. The debtor and nondebtor spouse filed post-petition separate income tax returns for a pre-petition tax year. The returns involved property which was the debtor's sole property or community property. The IRS issued separate refunds based on the returns and the bankruptcy trustee sought turnover of the refund sent to the nondebtor spouse. The court held that the refunds were estate property. The court held that the filing of the return for the refund was the responsibility of the trustee and the nondebtor spouse's filing for the return was a violation of the automatic stay. The court rejected the nondebtor spouse's argument that the turnover could not include the portion of the refund already spent. ***In re* Burke, 150 B.R. 660 (Bankr. E.D. Tex. 1993)**.

SOVEREIGN IMMUNITY. After the debtors received a discharge of all income tax liability, the IRS made several attempts to collect the discharged taxes. The debtors filed for an injunction and attorney's fees and costs incurred from the violation of the discharge. Even after the IRS was found to be in civil contempt for the post-discharge assessments, the IRS continued to seek payment and to offset refunds against the discharged taxes. Apparently, the IRS computer personnel refused or were unable to remove the debtors from the computer's delinquent files. The Court held that the IRS had waived its sovereign immunity by filing a claim in the original case and that under I.R.C. § 7430, the debtors were entitled to recover legal fees and costs incurred. ***In re* Abernathy, 150 B.R. 688 (Bankr. N.D. Ill. 1993)**.

TAX LIEN. The debtor sought to have a federal tax lien declared unsecured because the lien did not attach to the debtor's right to receive pension payments in the future and the pension payments were exempt. The court held that the tax lien attached to all of the debtor's interests in property, including the value of future payments from an existing pension plan, whether or not the property was claimed as exempt. The court also held that the lien was secured because the lien secured taxes less than the claimed value of the pension plan. ***In re* Cook, 150 B.R. 439 (Bankr. E.D. Ark. 1993)**.

FEDERAL AGRICULTURAL PROGRAMS

DAIRY TERMINATION PROGRAM. The plaintiff was a dairy farmer who enrolled in the Dairy Termination Program (DTP). The ASCS ruled that the plaintiff had violated the DTP contract in that two cows were not destroyed and were still being milked by a former employee of the plaintiff on another farm. Although the plaintiff pursued the ruling through DASCO and presented substantial evidence to refute the statements of the former employee as to how the cows escaped slaughter, the plaintiff was not allowed to cross-examine the former employee. The court first held that the DASCO decision was not reviewable de novo because the instant case was a review of an administrative decision and not a contract case. The court also held that the administrative appellate procedure was governed by the ASCS appeal regulations, 7 C.F.R. Part 780, and not the Administrative Procedures Act. However, the court held that the ASCS abused its discretion under Part 780 in not allowing cross-examination of the former employee, given the substantial contradictory evidence and the ASCS strong reliance on the former employee's statements in finding that the plaintiff had violated the DTP contract. In addition, in its remand order, the court required DASCO to make specific findings as to the knowledge of the plaintiff as to the removal of the cows by the former employer, because if the plaintiff did not know about the removal, the plaintiff could not be held in violation of the contract. DASCO failed to conduct a remand hearing within the allotted time and the plaintiff sought judgment on all issues in the plaintiff's favor. The court held that the plaintiff was entitled to judgment removing all penalties resulting from the adverse DASCO rulings. Because the plaintiff's right to contract payments required either an ASCS affirmative ruling of compliance with all contract provisions or a waiver of violations based on good faith compliance, the case was remanded to DASCO for such determinations; however, the court prohibited use of the former employee's testimony as support for any DASCO ruling. **Doty v. U.S., 27 Fed. Cl. (1993). See also Doty v. U.S., 24 Cls.Ct. 615 (1991)**.

NATIONAL FORESTS. The plaintiffs were injured while cutting trees under the employment of a company which contracted with the Forest Service to cull trees from national forests. The plaintiffs alleged that the Forest Service was negligent (1) in selecting contractors to cut the trees, (2) in selecting the trees to be cut and the method for cutting the trees, and (3) in failing to properly supervise the culling. The court held that because no specific regulations governed these Forest Service activities, the actions were discretionary and exempt from claims under the Federal Tort Claims Act. **Layton v. U.S, 984 F.2d 1496 (8th Cir. 1993), *aff'g*, 776 F.Supp. 1373 (W.D. Ark. 1991)**.

PERISHABLE AGRICULTURAL COMMODITIES ACT-*ALM* § 10.05[2]. The plaintiff was an officer and shareholder of a corporation subject to PACA and which from August 1987 through September 1987 purchased produce without making prompt payment. The plaintiff resigned by a letter dated October 1, 1987, but did not abandon the plaintiff's stock in the corporation. The plaintiff owned 10.5 percent of the stock and served as a director and vice-president and as manager for institutional sales during the period of the nonpayments. The failures to make prompt payment were found to be willful, flagrant and repeated violations of PACA. The USDA had determined that the plaintiff was "responsibly connected" with the corporation which would result in the plaintiff being barred from employment by a PACA licensee. The plaintiff argued that although the plaintiff's status in the corporation as officer, director and more than 10 percent shareholder fit the criteria of the statute, 7 U.S.C. § 499a(b)(9), the plaintiff, under *Quinn v. Butz, 510 F.2d 743 (D.C. Cir. 1975)*, should have the opportunity to prove that the plaintiff's actual connection to the corporation was only nominal. The court rejected the holding in *Quinn* and held that the statute established a *per se* rule and because the plaintiff had admitted being a director and officer of the corporation during several of the violations, the plaintiff was properly held to be responsibly connected with the corporation. **Faour v. U.S.D.A., 985 F.2d 217 (5th Cir. 1993)**.

PESTICIDES-*ALM* § 2.04. The plaintiff sued the manufacturers of a pesticide, methyl bromide, for personal injuries, alleging negligence, breach of warranty, and strict liability. The plaintiff alleged inadequacies of the use instructions, testing, research, labeling and warnings. The court held that under *Cipollone v. Liggett Group, Inc., 122 S.Ct. 2608 (1992) (federal cigarette labeling statute preempted state action involving labeling)*, FIFRA preempted the action insofar as the action related to labeling or warnings but allowed state court actions for breach of warranty. **Brennan v. Dow Chemical Co., 613 So.2d 131 (Fla. Ct. App. 1993)**.

The plaintiff filed a personal injury action in negligence, strict liability and breach of implied warranty for inadequate labeling against the manufacturer of pesticides used on dogs. The manufacturer moved for partial summary judgment on the inadequate labeling claims, arguing that the FIFRA preempted the state negligence action. The court agreed and held that the inadequate labeling action was barred by preemption of FIFRA. **Papas v. Upjohn Co., 985 F.2d 516 (11th Cir. 1993), *on rem. from*, 112 S.Ct. 3020 (1992), *vac'g and rem'g*, 926 F.2d 1019 (11th Cir. 1991)**.

FEDERAL ESTATE AND GIFT TAX

CHARITABLE DEDUCTION-*ALM* § 5.04[4]. Under the decedent's will, executed in 1976, two trusts were formed. The first trust provided for net income to be distributed for life to the decedent's servant with the remainder to pass to a charitable organization. The second trust provided for the servant's lifetime use of an apartment over a garage with the remainder of the property passing to a charitable organization. The trusts were amended to provide the servant with a fixed annuity payable from income and corpus, with the remainder to the charitable organization. The IRS ruled that the amended trusts qualified for the charitable deduction because the difference between the actuarial value of the qualified interest and the actuarial value of the reformable interest did not exceed 5 percent of the actuarial value of the reformable interest. **Ltr. Rul. 9312020, Dec. 24, 1992**.

INSTALLMENT PAYMENT OF ESTATE TAX-*ALM* § 5.05[1]. The decedent owned six apartment buildings and provided various services to the tenants either by the decedent or by employees. The IRS ruled that the services provided by the employees would be attributable to the decedent and the decedent's operation of the apartments was a trade or business such that the decedent's interest in the buildings qualified as a closely held business for purposes of paying estate tax by installments. **Ltr. Rul. 9311031, Dec. 18, 1992**.

VALUATION-*ALM* § 5.03. In April 1990, the taxpayer established a five year irrevocable grantor retained interest trust funded with nine pieces of artwork. The trust provided for all income to be distributed to the taxpayer at least annually with the remainder to pass to the taxpayer's issue per stirpes upon termination of the trust if the taxpayer was still alive. The trust also terminated upon the death of the taxpayer and the remainder then passed to the taxpayer's estate if the taxpayer died before April 1993; otherwise, the corpus passed to the taxpayer's issue. The trustee had the power to transfer or encumber the trust property and could leave nonproductive property in the trust. The taxpayer was allowed to display the artwork without charge. The IRS ruled that the value of the gift to the remainder holders was determined under I.R.C. § 7520 because the trust was established prior to the effective date of I.R.C. § 2702. The value of the taxpayer's retained interest was determined using 120 percent of the applicable federal rate for April 1990 for a person of the age of the taxpayer, 71, as 45.366 percent of the value of the property transferred to the trust. The gift was 54.364 percent of the value of the property transferred to the trust. **Ltr. Rul. 9313006, Jan. 6, 1993**.

FEDERAL INCOME TAXATION

COOPERATIVES-*ALM* § 14.03. A nonprofit, nonstock cooperative purchased and distributed products for franchised restaurants. The cooperative formed another nonprofit, nonstock corporation to assume the entire purchasing function for the franchises. The members of the new corporation included the cooperative and all franchise members. The IRS ruled that the new corporation operated on a cooperative basis because (1) it had democratic control in that all members had one vote and a majority of votes was needed to elect directors; (2) the corporation had subordination of capital in that all excess receipts above expenses were to be returned to the member patrons based on patronage; and (3) the allocation of excess revenues was made in proportion to the patrons' participation in the corporation. **Ltr. Rul. 9313016, Dec. 23, 1992**.

C CORPORATIONS

ACCUMULATED EARNINGS TAX. The IRS had assessed accumulated earnings tax (AET) against the corporate taxpayer based upon the undistributed earnings of the corporation and the net liquid assets which resulted from the sale of stock. The court found that the accumulation of liquid assets was not for tax avoidance but was a reasonable attempt to insulate the company from cash flow problems. The court held that because the net liquid assets were not accumulated for tax avoidance purposes, only the accumulated earnings could be considered in assessing AET. **Network Systems Corp. v. U.S., 93-1 U.S. Tax Cas. (CCH) ¶ 50,172 (D. Minn. 1993)**.

INVESTMENT TAX CREDIT-*ALM* § 4.04. The taxpayer was not allowed investment tax credit for the buildings that housed a car wash because the buildings were not an inherent part of the car washing machinery since the machinery could be replaced without replacing the buildings. **Schrum v. Comm'r, T.C. Memo. 1993-124**.

IRA. The taxpayer was the spouse and sole beneficiary of the decedent's IRA. At the date of the decedent's death, both the decedent and taxpayer were over 70 1/2 years of age. In the year of the decedent's death, the taxpayer rolled the decedent's IRA funds over to a new IRA owned by the taxpayer with distributions to begin in the following taxable year. The IRS ruled that the rollover was effective even though the taxpayer had already passed the required beginning date for minimum distributions. The IRS also ruled that no excise tax would be imposed for the year of the decedent's death for failure of the taxpayer to receive any distribution from the taxpayer's IRA because the taxpayer's IRA did not exist in the previous year. **Ltr.Rul. 9311037, Dec. 22, 1992**.

NET OPERATING LOSSES. The taxpayer was not allowed to revoke valid elections to carry forward net operating losses where although the return cited the incorrect code section, the other information submitted with the return demonstrated the intent to make the carryforward election. **Powers v. Comm'r, T.C. Memo. 1993-125**.

PARTNERSHIPS-*ALM* § 7.03.

ADMINISTRATIVE ADJUSTMENTS. The court held that the IRS was not barred by the statute of limitations from filing a final partnership administrative adjustment where the partnership had not filed returns for the taxable years involved. **Metals Refining Ltd. v. Comm'r, T.C. Memo. 1993-115**.

TAX SHELTERS. Limited partners were denied deductions for their share of partnership research and development fees, license fees and interest expenses because the partnership's putative business of exploiting a synthetic fuel process lacked economic substance. The court found that the partnership promoters' connections with the taxable entities involved with the partnership made the partnership's activites a sham with the only purpose of the partnership being to reap tax benefits. **Peat Oil & Gas Assoc. v. Comm'r, 100 T.C. No. 17 (1993)**.

PENSION PLANS. The IRS has issued guidance for direct rollover, 60-day rollover and 20 percent income tax withholding provisions for qualified pension plans under the Unemployment Compensation Amendments of 1992. **Notice 93-3, I.R.B. 1993-3**.

RETURNS. The IRS has announced corrections and changes on the worksheet on page 36 of Publication 535 for use in determining the deduction for medical insurance premiums for self-employed persons where (1) the taxpayer has more than one source of self-employment income, (2) the foreign earned income exclusion is claimed on Forms 2555 or 2555-EZ, or (3) the tapxayer's taxable year ends on a date other than December 31, 1992. **Ann. 93-53, I.R.B. 1993-14, 9**.

S CORPORATIONS-*ALM* § 7.02[3][c].

PASSIVE INVESTMENT INCOME. An S corporation had C corporation earnings and profits and had what was, at the time, considered passive investment income (interest) from lending customers money to purchase securities on margin. The corporation decided to distribute all of the C corporation earnings and profits but because it could not afford to do so, required the shareholders to recontribute the distributions except to the extent of the federal income tax on the distributions. Subsequently, regulations were issued which provided that the interest was not passive investment income. The IRS ruled that the distributions would not have qualified as effective to maintain the S corporation election; however, because the regulations were effective for the corporation's taxable year of the interest income, the corporation's election did not terminate because of excessive passive investment income. **Ltr. Rul. 9312027, Dec. 29, 1992**.

TERMINATION. An S corporation issued stock to an IRA of a shareholder without knowing that the transfer resulted in the termination of the S corporation election. The corporation repurchased the stock after learning from tax counsel that the transfer terminated the election. The IRS waived the termination as inadvertent, with the shareholder considered as owning the shares transferred to the shareholder's IRA. **Ltr. Rul. 9312018, Dec. 23, 1992**.

An S corporation issued stock to two partnerships which were ineligible S corporation shareholders. The S corporation stated that it had not intended to transfer the stock to the partnerships but had intended to transfer the shares directly to the individual partners. After some delay, the shares were transferred to the partners. The IRS waived the termination of S corporation status as inadvertent and required the partnerships to be treated as the shareholders for the period in which the partnerships owned the stock. **Ltr. Rul. 9312021, Dec. 24, 1992**.

TRUSTS. A shareholder of an S corporation transferred shares to an irrevocable trust for five beneficiaries, each with an equal share in the trust. The trust did not file an election to be treated as a QSST because of advice from legal counsel that the election was not needed. The trust provided for separate equal shares with each share receiving one-fifth of the net trust income at least annually. Each beneficiary was to receive the share of trust corpus at age 30. The IRS waived the termination of the S corporation election as inadvertent and ruled that the trust qualified as a QSST, treating each share as a separate trust. **Ltr. Rul. 9313011, Dec. 18, 1992**.

WITHHOLDING TAXES-*ALM* § 4.06. The plaintiff was a trucking company which provided its employee truck drivers with the opportunity to obtain advance payments of their compensation for "personal expense" while on the road. The taxpayer also included reimbursements for travel expenses to drivers for past expenses but did not separately identify the travel expenses when the amounts were paid. The court held that under Treas. Reg. § 31.3121(a)-1(h), the advance payments were not wages subject to FICA withholding because the advance payments were made separately and were made for reasonable travel expenses. The other payments were wages because not made separately nor identified as reimbursed travel expenses. **Boyd Bros. Transp. Co., Inc. v. U.S., 27 Fed. Cl. 509 (1993)**.

LANDOWNER'S LIABILITY

RECREATIONAL USE-*ALM* § 1.02[1]. The plaintiff was injured while riding on a three-wheeled cycle on the defendant's farm. The defendant's dog had been chasing the cycle and the driver ran into a fence when trying to avoid hitting the dog. The plaintiff argued that the "dog bite statute" applied to make the defendant liable for the acts of the dog. The court held that the playful actions of a dog did not make the owner liable under the statute which applied only to vicious attacks by dogs. The plaintiff also argued that the defendant was not protected by the recreational use statute because the defendant did not allow the general public to use the farm for recreational purposes. The court held that the recreational use statute did relieve the defendant of liability because the statute required only that the defendant allow some members of the public to use the land. **Holden v. Schwer, 495 N.W.2d 269 (Neb. 1993)**.

PRODUCT LIABILITY

TRACTOR-*ALM* § 1.02[4]. The plaintiff's decedent was killed when the farm tractor the decedent was operating rolled over as the decedent drove the tractor down a steep hill. Although the tractor was available with a roll over protective system (ROPS), the purchaser, the decedent's employer, did not purchase the tractor with the ROPS. The plaintiff sued the manufacturer for breach of implied warranting of merchantability for failing to have a ROPS, for negligence and breach of implied warranty of merchantability for failure to warn about operating the tractor on steep hills, and negligent design. The court upheld summary judgment for the defendant. The court held that no breach of implied warranty of merchantability occurred because of the failure of the tractor to have a ROPS because the ROPS was available but the tractor was not purchased with the ROPS. Although the court rejected the defendant's argument that it had no duty to warn about open and obvious dangers, the court held that the failure to warn was not an approximate cause of the decedent's death where the decedent had been warned about the danger of driving on steep hills and the lack of a ROPS was obvious. The court also held that the tractor was not negligently designed because the tractor was available with a ROPS and the purchaser voluntarily purchased the tractor without the ROPS. The court rejected the plaintiff's argument that the manufacturer had a duty to "retrofit" the tractor to increase the roll over protection. **Butler v. Navistar Intern. Transp. Corp., 809 F. Supp. 1202 (W.D. Va. 1991)**.

RIPARIAN RIGHTS

NUISANCE. The plaintiff owned land across from and downstream for the defendant. The defendant conducted earthwork projects which the plaintiff claimed caused the river to flood onto the plaintif's land. The nearby city had sought to have the work declared in violation of a city ordinance and a public nuisance. The plaintiff argued that because the earthwork violated the city ordinance, the work was a private nusiance by law subject to abatement. The court held that the plaintiff must also show that the violation of the ordinance caused harm to the plaintiff. The court reversed the jury verdict for the defendant because the jury instructions implied that the defendant had the right to take whatever action was necessary to protect the property from flooding, whereas the law allowed the defendant only to restore the river bank to its original condition or to return the river to its original course. **Smicklas v. Spitz, 846 P.2d 362 (Okla. 1992)**.

STATE TAXATION

VALUATION. The plaintiffs contested the valuation of their ranch land for property tax purposes. The plaintiffs argued that the valuation was arbitrary and capricious because the valuation did not account for the failure of the plaintiffs to make any profit from the land. The Appraisal District had used cash leases of comparable property near the plaintiff's land to determine the value of the plaintiff's land. The court held that the valuation statute and regulations did not allow consideration of the individual owner's inability to make a profit from the land and upheld the valuation. **Walker v. Appraisal Review Bd., 846 S.W.2d 14 (Tex. Ct. App. 1992)**.

SECURED TRANSACTIONS

FEDERAL FARM PRODUCTS RULE-*ALM* § 13.01[4][a]. The plaintiff bank had a perfected security interest in cattle purchased by the debtor for feeding and resale. The debtor sold the cattle to the defendant but failed to make payment of the loan secured by the cattle. The bank sought return of the cattle from the defendant based upon its priority security interest. The bank claimed that the federal farm products rule did not apply because the defendant did not purchase the cattle in good faith and because the cattle were not farm products since the cattle were not raised by the debtor. The court held that the federal farm products rule had no good faith purchase requirement and that cattle fed by the debtor engaged in a cattle feedlot operation were farm products. Because the state did not have a certified central filing system and the bank failed to give the required notice of its security agreement, the defendant took title to the cattle free of the security interest. **Asburn Bank v. Farr, 426 S.E.2d 63 (Ga. Ct. App. 1992)**.

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SUBORDINATION. One of the debtor's creditors had obtained a perfected security interest on the debtor's farm equipment. The debtor sought an FmHA loan but the FmHA required that the debtor obtain subordination of the creditor's security interest so that the FmHA security interest on the equipment would have priority. The FmHA entered into a subordination agreement with the creditor but the agreement did not specifically require subordination of the creditor's security interest on the equipment, although the agreement referred subordination of the creditor's "mortgages." At the closing, the FmHA sent a transmittal letter requesting the creditor to release its lien on the equipment but the creditor did not do so. The court held that the subordination agreement did not subordinate the creditor's security interest in the farm equipment because the agreement did not specifically mention the security interest nor did any of the extrinsic evidence indicate that the parties intended the agreement to cover the security interest in the equipment. **U.S. v. Haas Fruit, 812 F. Supp. 173 (E.D. Wash. 1993)**.

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